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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1992

CITY OF CHANUTE, KANSAS, *et al.*,
*Petitioners,*

v.

WILLIAMS NATURAL GAS COMPANY,
*Respondent.*

**On Petition for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit**

## REPLY BRIEF OF PETITIONERS

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## REPLY BRIEF OF PETITIONERS

Respondent Williams Natural Gas Company's ("WNG") brief in opposition, despite its improper reliance on contested issues of fact, concedes basic matters which underscore the importance of this Court granting *certiorari* to correct fundamental errors of law committed by the circuit court below, which immunize the nation's interstate pipeline companies from antitrust liability. First, while conceding that nothing in the "regulatory regime of the Natural Gas Act . . . and the Natural Gas Policy Act of 1978 'immunizes' WNG from the antitrust laws," (WNG Br. at 2) and not contesting the court's finding that it had monopoly power in the relevant market under § 2 of the Sherman Act through control of its interstate transmission facilities (App. 21a), WNG inconsistently argues that the circuit court properly affirmed, as a matter of law, that such an interstate pipeline can refuse to transport through its facility gas purchased by distributors in competition with it from independent producer sources at low market prices, as long as the pipeline agrees to sell its own gas at FERC regulated prices. WNG Br. at 15. But this is in essence a thinly veiled regulatory immunity argument, uniformly rejected by this Court and other courts.

WNG's further contention that the antitrust laws do not apply because of its transmission of gas from certain other restricted sellers at above market prices is equally wrong. WNG Br. at 16-17. By including these other sellers (under FERC Order No. 451, 51 Fed. Reg. 22,168 (1986) ("Order 451"), WNG in effect concedes that the court's logic below was not premised on WNG's sales of its own gas at FERC regulated prices, but on the idea that immunity exists simply where WNG sells or transmits any gas at any price. If a monopolist can use its essential facility to force the purchase of its own or other similarly high priced gas and thereby obtain immunity from § 2 of the Sherman Act to enable it to bar access by distributors in competition with it to available low priced supplies of gas, the antitrust laws will have become meaningless. Thus, the circuit court decision below should be reviewed because of its adverse

impact on the applicability of § 2 of the Sherman Act in the increasingly important realm of competitive dealings between producers and purchasers of natural gas vitally dependent on transmission by interstate pipelines at the national level.

Secondly, WNG concedes that the court of appeals erred in holding that a § 1 claim under the Sherman Act for illegal tying cannot be found in the arrangements and contracts between the Cities and WNG. WNG Br. at 18. This admittedly defective key ruling by the Tenth Circuit below is important because it would exempt virtually all tying arrangements between an interstate pipeline and its distributors or other customers, treating such agreements as "unilateral conduct" outside the scope of Sherman Act § 1. WNG's attempt to revive the court's holding by reliance on the concurring opinion of one of the judges (who disagreed with the majority on this issue) is legally defective, because the majority did not accept or expressly agree with the suggested alternative. App. 13a. Furthermore, the alternative, i.e., that the existence of Order 451 gas precluded any claim that WNG "forced" the Cities, by closing its pipeline, to purchase WNG's gas, is factually and legally defective. Not only was the first Order 451 gas available months after WNG had closed its pipeline and forced the Cities' new arrangements with it (App. 6a), but also WNG's conduct in closing the pipeline forced the subsequent availability of that Order 451 gas to be priced at a high level closely approximating WNG's own price, so that the Cities were still forced into an unacceptable, anticompetitive, high priced "alternative" which provided them no effective relief in their ability to compete with Williams in the relevant market.

Third, WNG's urging that the court of appeals properly held that WNG's conduct, as a matter of law, was motivated by legitimate business justification, directly conflicts with WNG's concession that it had no "full requirements" contract with at least five of the Cities before or during all of the closed period. WNG Br. at 25. This requires setting aside the summary judgment against all eight Cit-

ies. The majority opinion expressly ruled that its grant of summary judgment against all the Cities, based on its ruling of law that WNG had a "legitimate business justification," was premised solely on the court's conception that the Cities had full requirements contracts with WNG. App. 24a. The majority itself expressly conceded that without the existence of such contracts, a point now conceded by WNG in its brief, this Court's opinion in *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973) would control and summary judgment should be denied. App. 24a. Furthermore, the majority of the court below also cited *State of Illinois v. Panhandle Eastern Pipe Line Co.*, 935 F.2d 1469 (7th Cir. 1991), *cert. denied*, ___ U.S. ___ (1992), a case relied upon by WNG, as similarly holding that a valid business justification can exist only where full requirements contracts are in place between the pipeline and its customers while it closed its pipeline. App. 24a.

In sum, the circuit court's decision effectively denies access to federal courts for antitrust claims on three major antitrust premises, i.e., monopoly control under § 2 relating to essential facilities, tying agreements under § 1, and rulings of law as to legitimate business justifications. These are significant to producers, pipelines and consumers and go to the heart of the proper administration of the federal antitrust laws, this Court's decisions and sound public policy. The Tenth Circuit decision, involving sweeping, wide-ranging changes in the existing application of the federal antitrust laws to this important area involving approximately 30 percent of the nation's energy supply, should be reviewed.

1. WNG's response to the Cities' analysis that the court of appeals had improperly negated § 2 of the Sherman Act and the essential facilities doctrine by the unique ruling that the owner of such a facility can bar its use for transmission of alternate lower cost competitive supplies of gas by simply offering to sell its own gas, regardless of price, is patently fallacious. WNG alleges "a fundamental distinction" between this case and *Aspen Highlands Skiing Corp. v. Aspen Skiing Co.*, 738 F.2d 1509 (10th Cir. 1984),

*aff'd*, 472 U.S. 585 (1986), *Otter Tail*, and *MCI Communications Corp. v. American Tel. & Tel. Co.*, 708 F.2d 1081 (7th Cir.), *cert. denied*, 464 U.S. 891 (1983) on the ground that in each of these cases the defendant's conduct completely excluded the plaintiff from the market in which they competed. WNG. Br. at 13-14. This is a plain misreading of the cases. In *Aspen*, the defendant did not completely exclude the defendant from participating in a multi-mountain arrangement for ski tickets, but set the pro rata share allocated to the plaintiff so low as to impair the economic viability of the proposal to the plaintiff. *Aspen Skiing*, 472 U.S. at 590-92, 608-09. In *Otter Tail*, the defendant refused to wheel a lower cost wholesale supply of power to the plaintiff cities, while it did offer to sell its own power at retail under regulated prices to serve customers in each of the cities. *Id.*, 410 at 368. The Tenth Circuit's decision conflicts with *Otter Tail* because that case firmly holds that the existence of regulated services does not, standing alone, provide reasonable access sufficient to justify the company's refusal to transmit power over its lines.[1]

Similarly, in *MCI*, the Seventh Circuit directly overruled the defendant's contention that since its connection services were regulated, the defendant's refusal to give plaintiffs access to alternate long distance services could not constitute a violation of the essential facilities doctrine. *MCI*, 708 F.2d at 1101-1105. In each of these cases, the defendant denied access to essential facilities owned and controlled by it for transporting or making available

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[1] WNG alleges that *Otter Tail* is not an "essential facilities case." WNG Br. at 14 n.10. While it is true that the term "essential facilities" was not used, commentators and courts alike have described *Otter Tail* as an essential facilities case. *See*, e.g. Areeda & Hovenkamp, *Antitrust Law*, ¶ 736.1 (Supp. 1989) at pp. 699, 708; Olympia Equip. Leasing Co. v. Western Union Tel. Co., 797 F.2d 370, 376 (7th Cir. 1986), *cert. denied*, 480 U.S. 934 (1987). By the same token, while this court in *Aspen* discussed the issue using principles and language of Section 2 of the Sherman Act, the court's analysis covered all of the substance of the antitrust issues which this Court and the circuit courts have focused on in describing the "essential facilities doctrine."

plaintiff's own product, thereby requiring the plaintiff to use the defendant's product. This is identical to WNG's denial of use of its transmission system for the Cities own gas, thus forcing the use of WNG's gas.[2]

Furthermore, the concept espoused by WNG, that the antitrust laws only apply to conduct which completely excludes the plaintiff from the market, wrongfully characterizes established antitrust law holding that a refusal to deal, except on unreasonable terms, includes conduct short of total exclusion. *Delaware & Hudson Railway Co. v. Consolidated Rail Corp.*, 902 F.2d 174, 179-180 (2d Cir. 1990), *Consol. Gas of Fla. v. City Gas Co.*, 665 F. Supp. 1493, 1534-35 (S.D. Fla. 1987), *aff'd en banc*, 912 F.2d 1262 (11th Cir. 1990). Accordingly, the court of appeals erred in deciding that "[a]s a matter of law, we find Williams' supply of gas at FERC approved prices provided the Cities with reasonable access to the pipelines." App. 9a.

WNG's alternate contention, that the Cities' essential facilities claim fails because of the availability of Order 451 gas from WNG, is legally and factually defective. WNG's offer of Order 451 gas is indistinguishable from WNG offering its own gas. In both cases, the gas being offered to the Cities by WNG expressly excluded the Cities' ability to receive transmission of their own purchased gas supply which had been negotiated independently under competitive conditions from alternative gas suppliers. Loss of Cities' OWN gas supply directly impaired the Cities' ability to compete with WNG. The established facts of record, not challenged by the Tenth Circuit in its opinion, had been set forth earlier by the district court in granting a preliminary injunction to the Cities, namely, that because

[2] WNG argues that the Cities competed with WNG for retail customers and, because Cities were able to serve their retail customers (albeit not by using their own gas but by being forced to buy WNG's gas), no violation occurred. Under this theory, had the Cities in *Otter Tail* been forced to allow the defendant to serve the retail customers in the Cities, there would have been no antitrust violation from the defendant's refusal to deal. Such a proposition is clearly inconsistent with the rationale and holding of *Otter Tail*.

of the lack of competition resulting from WNG's closing the pipeline, the Order 451 gas was priced only a few cents lower than WNG's own price, and that regardless of price, the Order 451 supply was interruptible, in large blocks, and did not meet the Cities' smaller firm gas requirements. App. 6a, App. 146a.[3] Furthermore, Order 451 by its terms was not applicable to those Cities whose existing gas purchase contracts with WNG had expired.[4] WNG rightfully concedes that the FERC's regulations dealing with Order 451 gas provided only WNG's "firm sales customers" with a right of first refusal to purchase gas. WNG Br. at 12. This fact alone bars the court's summary judgment against all of the Cities based on Order 451. But regardless of this, WNG's offering of 451 gas at an admitted price substantially in excess of the price that the Cities obtained in their contracts with outside third party gas sellers, directly impaired the Cities' ability to compete with WNG in the market. *See* App. 145a-146a. Thus, WNG's refusal to transport the Cities' gas denied them access on reasonable terms and conditions to the essential facilities. *United States v. Terminal R.R. Ass'n*, 224 U.S. 383, 411 (1912).

But no matter how the ruling is characterized, its breadth and importance cannot be doubted. By holding as a matter of law that a pipeline having monopoly power through its control of an essential facility can close its line to transportation of competitive supplies purchased and

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[3] As the circuit court below confirmed (App. 6a):

> The approved third party suppliers' gas that Williams continued to transport was short term and interruptible,[6] whereas the other third party suppliers provided long term, firm and much cheaper gas.[7] *Id.* at 1521.

[6] Interruptible service does not guarantee that a producer will have sufficient supplies of natural gas to meet all consumers' demands.

[7] Firm service does guarantee that consumers' demands will be met.

[4] *See* FERC Regulations, 18 C.F.R. § 270.201(g)(1)(ii).

owned by distributors in competition with the pipeline, by the simple expedient of offering only its own gas or similar higher-priced gas (*see* App. 6a), poses a widespread national issue, an issue important to the day-to-day business dealings between interstate pipelines and those selling or purchasing gas dependent on transmission through the pipeline's facilities.

2. WNG does not even attempt to defend the majority opinion on the tying issue. WNG Br. at 18. The court's holding, that a contract between a buyer and a seller is not a tying contract in violation of § 1 because it lacks the required multiplicity of parties, conflicts with decisions as old as *International Salt Co. v. United States*, 332 U.S. 392 (1947), and as recent as *Eastman Kodak Company v. Image Technical Services, Inc.*, ___ U.S. ___, 60 U.S.L.W. 4465 (1992) and numerous decisions in the interim. Petition at 17-20. This Court should not allow such a bad precedent to remain uncorrected.

WNG's attempt to salvage this issue by asserting that the majority's summary judgment can be upheld on the alternate ground that the Cities were not *forced* to purchase WNG's sales gas because of the availability of Order No. 451 gas, is both legally and factually deficient. First, WNG's claim is legally defective because the majority opinion denied the Cities' tying claim under § 1 of the Sherman Act solely on the ground "that a tying arrangement imposed by a single entity is not proscribed by § 1 of the Sherman Act." App. 12a. The majority never decided the Cities' claim of error regarding "forcing" of a tying arrangement, deeming that to be a moot question in view of its decision on the single entity issue. App. 13a at fn. 11. Not having decided the forcing issue, it was impermissible speculation on behalf of the concurring judge to so conclude. App. 30a-32a. Furthermore, the concurring judge was in error on the record. When WNG closed down its pipeline on August 1, 1987, there were no available supplies of Order 451 gas for a number of months and all of the Cities were forced to take WNG's gas in the interim. Thereafter, Order 451 gas was available only to pipeline

customers with existing firm requirements contracts. WNG Br. at 12, II FERC Regulations (CCH) ¶ 24,051 at 14,115, 18 C.F.R. ¶ 270.201(g)(1)(ii) (1987). Thus, the five Cities with the expired contracts had no "right" to "force" WNG to transport Order 451 gas for all or part of the year the pipeline was closed.

3. WNG's contention that "the only evidence in the record is that WNG's actions were justified by legitimate business reasons warranting summary judgment for WNG" flagrantly misstates substantial contrary evidence confirmed by the court of appeals below. *See* App. 6a-7a, 19a-21a. The court concluded that Cities had established "Williams has monopoly power in the relevant market" (App. 21a); that the Cities' evidence showed WNG was confronted only by a modest $12.1 million take-or-pay exposure (App. 20a); and that WNG in fact had closed its pipeline to enhance its higher profits from sales (App. 20a).[5] But the Court went on to hold as a matter of law that because "Williams . . . wanted to prevent conversion of sales service to transportation service" Williams' refusal to provide access was justified by "Williams' legitimate business concerns."

> . . . The Cities argue Williams' low take-or-pay liability cannot be characterized as a legitimate business concern sufficient to justify closing the pipeline. Perhaps that argument would fly if that were the only evidence of concern, but evidence exists Williams also wanted to prevent conversion of sales service to transportation service. Consequently, we hold refusal to provide access can be justified by Williams' legitimate business concerns. . . .

App. 23a. The lynch pin of the court's holding on the intent issue was its finding that WNG had existing full

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[5] WNG improperly tries to argue that it made no more profit on sales than transportation (WNG Br. at 22), a proposition refuted by its Annual Report to Stockholders. App. 20a.

requirements contracts with all of the Cities in place which justified it making the business decision to close the line.

> The Cities rely on *Otter Tail Power Co. v. United States*, 410 U.S. 366 . . . for the proposition an asserted business justification must be procompetitive to withstand judicial scrutiny. In *Otter Tail*, an electricity producer's refusal to transport electricity over its lines (wheeling) to towns with which its contracts had ended violated § 2 of the Sherman Act. A similar argument was raised in *Panhandle*, *Panhandle*, 935 F.2d at 1485. However, the *Panhandle* court found the existence of extant contracts with its natural gas customers distinguished the cases. Similarly, as noted above, we found the full requirements provision of the contracts to be in full force when the pipeline was closed. . . .

App. 24a.

Thus, under the Tenth Circuit's own rationale, a valid business reason exists where prior full requirements contracts exist, otherwise a contrary result would be reached under *Otter Tail*. The fatal error made by the Tenth Circuit below was its assumption that WNG had full requirements contracts with all of the Cities. However, as WNG conceded in its brief, five of the eight Cities' prior full requirements contracts had expired either before or during the relevant time period. WNG Br. at 25. Accordingly, based on the very rationale that the circuit court below employed, it was impossible for the court to validly conclude as a matter of law that summary judgment could be granted based on asserted business justification as to those Cities with expired contracts. To the contrary, as the Tenth Circuit clearly conceded, *Otter Tail* controlled so that a utility's refusal to transport electricity over its line to towns "with which its contracts had ended violated § 2 of the Sherman Act."[6]

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[6] WNG's second argument, that it did not close its pipeline in order

Furthermore, the court of appeals below clearly erred as a matter of law in holding that even though the evidence by the Cities showed that WNG's shut down was motivated by the desire to increase its profits from sales and to force the Cities into remaining as sales customers of WNG, this constituted a valid "business reason" to exonerate it under § 2. App. 23a-24a. This flies in the face of all of the decisions from *Otter Tail*, *Aspen*, and *MCI*, condemning such a clear abuse of monopoly power by a monopolist to enhance its monopoly position not through business acumen, but through bald anticompetitive domination.[7]

## CONCLUSION

For the foregoing reasons, Cities urge that their petition for a writ of certiorari be granted.

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to cause Cities to sign new long-term sales contracts, WNG Br. at 21-22, also relies on disputed factual issues. City officials submitted affidavits that WNG officials told them that WNG's purpose in closing the pipeline was to force WNG's customers, including Cities, to sign new long-term sales contracts with WNG. *See* App. 23a-24a.

[7] Contrary to the decision below, where the desire for higher profits is obtained from abuse of monopoly power, it is not and should not be a legitimate business justification. Delaware and Hudson Railway Co. v. Consolidated Rail Corp., 902 F.2d 174, 178 (2d Cir. 1990) ("a monopolist cannot escape liability for conduct that is otherwise actionable simply because that conduct also provides short-term profits.")

WNG's argument that Cities are precluded from relying on the coercion in this case because Cities previously lost a coercion argument before FERC WNG Br. at 22 n.13, is a serious misrepresentation. None of the nine Kansas Cities that were allowed to intervene in that FERC case are parties in this antitrust case. *Williams Natural Gas Co.*, 44 F.E.R.C. ¶ 61,009 at 61,039 n.3 (1988).

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